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United States Bankruptcy Court
Albuquerque, New Mexico

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

In re

FURR'S SUPERMARKETS, INC.,

Debtor.

Case No. 11-01-10779-SA
Chapter 11

DEBTOR'S REPLY TO OBJECTIONS TO APPLICATION
<u>TO RETAIN PETER J. SOLOMON COMPANY LIMITED</u>

<u>Introduction</u>

This matter turns on two issues. First, is it unreasonable to tell a professional at the outset of an engagement what its compensation structure will be for the task performed? Or must the professional wait until the end of a chapter 11 case to find out what, if anything, the professional "deserves" for its efforts?

Second, should a professional be compelled to face uninsured and uncompensated risks just because the chapter 11 case has been filed? Or is the professional entitled to the same protection against frivolous suits that it receives in every other engagement?

The Debtor has demonstrated the reasonableness of Peter J. Solomon Company Limited's ("PJS") proposed fees, and the terms of PJS's proposed engage-

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ment are both prosaic and entirely proper. The Court should approve the Debtor's application to retain PJS at its usual rates and terms, and overrule the Objections in their entirety.

I. Under 328(a) A Professional May Be Employed on Any Reasonable Terms and Conditions of Employment

Under section 328(a), professionals may be employed and compensated "on any reasonable terms and conditions of employment, including on a retainer, on an hourly basis, or on a contingent fee basis."[1] Once approved, the professional may rely upon compensation according to the approved terms, unless they prove to have been improvident in light of developments unanticipated at the time of entry of the retention order.

The statute's plain language contemplates a variety of retention arrangements and allows professionals to know what they will be paid before beginning work. While the Objectors may prefer to examine PJS's compensation only with the benefit of hindsight, Congress permitted otherwise. Accordingly, the only issue is whether the PJS retention agreement provides for "reasonable terms and conditions of employment."

Paragraphs 10 through 14 of the Supplemental Declaration of Bradley I. Dietz, dated May 3, 2001 (the "Dietz Declaration"), address the reason-

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[1] 11 U.S.C. § 328(a).

ableness of PJS's proposed compensation. The table annexed to the Dietz Declaration as Exhibit A reports the monthly and restructuring fees charged by investment bankers in fifteen comparably-sized chapter 11 cases. A sizable binder of retention papers from comparable engagements was also submitted in support of the Application. Taken together, these documents show "the projected salaries of participating professionals, billing rates and prevailing fees from comparable engagements,"[2] and demonstrate that PJS's proposed engagement is under reasonable terms and conditions, as required by section 328(a) of the Bankruptcy Code.

That the Committee can find four supermarket bankruptcy cases (reported on Committee Exhibit B) that produce an average lower than the PJS's proposed compensation is irrelevant, especially when one of the cases is five years old. An average based on a sample size of four is hardly significant, and inducing the conclusion that PJS's fees are excessive based on such a sample is inherently risky.

Simple statistical analysis illustrates the point. If investment banker fees are normally distributed, the most that can be deduced from the Committee's exhibit is that average total investment banker fees in supermarket cases should fall

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2 *In re Drexel Burnham Lambert Group, Inc.*, 133 B.R. 13, 27 (Bankr. S.D.N.Y. 1991).

between 0.21% and 2.49% of transaction value.[3] The Committee reports that PJS's total proposed fees fall between 1.6 to 1.8% of transaction value. Thus, by the measure of the Committee's own exhibit, PJS's proposed fees are reasonable.

The Committee's reliance on the case analysis attached to the in *In re VF Brands, Inc.* retention application, which the Committee submits as Exhibit C, again places excessive faith in averages. The investment banker in the *VF Brands* case requested and received approval of compensation that exceeds both the average on the chart and PJS's requested compensation in this case.

More importantly, the Bankruptcy Code does not require that professionals charge a standardized, average rate. Instead, the Code simply requires that a professional's compensation be reasonable. As demonstrated by the exhibits and declarations submitted in support of the Application, PJS's proposed terms are comparable to those used by investment bankers in other large chapter 11 cases. Accordingly, the Debtor is entitled to retain PJS on those terms in its bankruptcy case.

PJS does not seek to use section 328(a) to avoid its obligation to file fee applications under section 330, or otherwise deprive the Court of authority over

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3 Based on the following calculation (know as the "student's t"): 1.35 (the average) ± 3.18 (critical value, $t_{.025}$) * [0.72 (the standard deviation) ÷ 2 (the square root of the number of observations)].

the professionals retained in this case.[4] PJS will file fee applications, but approval of the retention agreement under 328(a) will allow PJS to know in advance what its compensation structure will be. Congress plainly anticipated that professionals would be provided with this knowledge – section 328(a) would have no meaning if this were not so. The Debtor has shown that PJS's retention agreement provides for "reasonable terms and conditions of employment," as required by section 328(a) of the Bankruptcy Code, and the Debtor's employment of PJS should therefore be approved.

II. There Is No Prohibition – in or out of Bankruptcy – Against the Indemnification of Non-Attorney Professionals

The United States Trustee's fusillade against indemnification – which the Committee audaciously joins, despite its pending application to provide its investment banker with equivalent indemnification protection – suffers from two rudimentary flaws. First, any fiduciary duty that bankruptcy professionals owe is to the debtor, not the creditors at large.[5] The Trustee's attempt to expand the

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[4] *See generally*, Robert J. Landry & James R. Higdon, *A Primer on 11 U.S.C. § 328(a) and its Use in Alternative Billing Methods in Bankruptcy*, 50 MERCER L. REV. 537 (1999).

[5] *See Hansen, Jones & Leta v. Segal*, 220 B.R. 434, 458 (D. Utah 1998) ("Certainly equating the statutory duties of counsel with those of the client, whether debtor-in-possession or trustee, is inconsistent with the Bankruptcy Code.").

duties of bankruptcy professionals – by creating a daisy chain of fiduciary duties[6] – should be rejected out of hand.

Second, cases prohibiting the indemnification of attorneys or underwriters are inapposite, and do not support the notion that no professional may ever be indemnified. Attorneys are subject to regulation by the various state bars, which have generally prohibited attorney indemnification.[7]

Investment bankers plainly are not subject to such regulation. The Tenth Circuit, in an unpublished opinion, has rejected efforts to impose an attorneys' unique duties on non-legal professionals,[8] and this Court should similarly reject the Objectors' attempts to impose the attorney regulatory scheme on non-legal professionals.

Cases disapproving indemnification for underwriters, on the other hand, involve attempts to indemnify underwriters for their violation of Federal

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6 *E.g.*, U.S. Trustee Brief, page 10.

7 *E.g.*, CALIFORNIA RULES OF PROFESSIONAL CONDUCT Rule 3-400(A); MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.8(h); MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 6-102.

8 *Amdura Nat'l Distribution Co. v. Deloitte & Touche (In re Amdura Corp.)*, 1994 WL 596777, *1 (10th Cir. Nov. 2, 1994) ("We decline [the] invitation to adopt a new rule of law that would impose on an accounting firm a duty of advocacy commensurate with that of an attorney or trustee.").

Securities Laws.[9] Just as the Debtor could not indemnify PJS for violations of New Mexico criminal statutes, the quasi-penal nature of the Federal Securities Laws plainly implicate a host of public policy concerns not present in a simple attempt to indemnify an agent that is found negligent.

Without the ill-founded notions that a debtor's professionals owe a fiduciary duty to the creditors at large or that indemnification of professionals is *per se* inappropriate, the United States Trustee's eclectic collection of state law decisions limiting indemnification in landlord-tenant relationships,[10] personal-investment-advisor agreements,[11] and home-health-care-provider contracts[12] is left without a mooring. The undertone of overreaching and unequal bargaining power found in these decisions is absent in an agreement between a multi-million dollar

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9 *E.g., Eichenholtz v. Brennan*, 52 F.3d 478 (3rd Cir. 1995).

10 *Borg-Warner Ins. Finance Corp. v. Executive Park Ventures*, 400 S.E.2d 340 (Ga. App.1990) (indemnification unenforceable, statute prohibited indemnification for acts resulting in bodily injury).

11 *Erlich v. First Nat. Bank of Princeton*, 505 A.2d 220 (N.J. Super. Law Div. 1984) (in the context of an investment management account, bank could not rely upon an exculpatory clause to relieve itself from liability for its own investment decisions); *see also St. Paul Fire and Marine Ins. Co. v. Wells Fargo Alarm Services*, 1995 WL 306642, at * 2 (D.N.J. May 09, 1995) ("Under New Jersey law, exculpatory clauses in private contracts are generally enforceable unless a party to the contract is either under a public duty entailing the exercise of care, such as a common carrier or public utility, or if there is unequal bargaining power between the parties.").

12 *Rosenthal v. Bologna*, 620 N.Y.S.2d 376 (App. Div. 1995).

corporation and its investment banker, and, moreover, many of the cases the Objectors rely upon do not support the *per se* bar on indemnity that the Objectors urge. As the Supreme Court of Wisconsin noted in a case quoted by the United States Trustee:

> Exculpatory contracts are not favored by the law because they tend to allow conduct below the acceptable standard of care. *However, exculpatory contracts are not automatically void and unenforceable.* Rather, a court closely examines whether such agreements violate public policy and construes them strictly against the party seeking to rely on them.[13]

Investment bankers use indemnification to deter parties from bringing meritless suits against a "deep pocket" in the hopes of coercing a settlement. This is especially important in bankruptcy engagements, where the divisive nature of the proceedings may often produce one or more parties disappointed by the outcome of the case.

PJS does not include the cost of insuring against the threat of litigation in setting its fees, and does not insure against potential litigation. Without indemnification, PJS would be exposed to uninsured and uncompensated risks. There is no support in the Bankruptcy Code for the contention that PJS should have

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13 *Yauger v. Skiing Enterprises, Inc.*, 557 N.W.2d 60, 62 (Wis. 1996) (emphasis added & citations omitted). Further, Wisconsin's "strict" approach to indemnity clauses is not uniformly followed throughout the nation. *See, e.g.*, *Keating v. United Instruments, Inc.*, 742 A.2d 128, 133 (N.H. 1999) (comparing New Hampshire, Texas and Kansas law, and noting that "each of these States has different requirements for construing indemnification agreements as they relate to the indemnitee's own negligence.").

to endure this risks simply because its client is in bankruptcy. Bankruptcy decisions that hold otherwise "overlook the common law principles permitting indemnity of fiduciaries, and the idea that a fiduciary cannot be indemnified for negligence, or that such indemnification is contrary to public policy, is just plain wrong."[14]

The Debtor has determined that it is in the best interest of the estate to retain PJS under terms that are standard, and enforceable, outside of bankruptcy. The Court should reject the proposition that professionals cannot be indemnified for negligence.

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14 *In re Joan and David Halpern, Incorporated*, 248 B.R. 43, 46 (Bankr. S.D.N.Y. 2000), *aff'd*, 2000 U.S. Dist. LEXIS 17589 (S.D.N.Y. Dec. 6, 2000).

CONCLUSION

The Court should overrule the Objections and grant the full relief requested in the Application.

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